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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959.

No. 842

UNITED STATES RUBBER COMPANY,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

D. NELSON ADAMS,
Counsel for Petitioner,
15 Broad Street,
New York 5, N. Y.

JOHN A. REED,
RICHARD R. DAILEY,

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UNITED STATES RUBBER COMPANY,

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COMMISSIONER OF INTERNAL REVENUE,

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

TO THE HONORABLE THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Petitioner respectfully asks that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Second Circuit dismissing for lack of jurisdiction a petition to review the decision of the Tax Court of the United States.

Opinion Below.

The opinion of the Court of Appeals is reported in 274 F. 2d 307 and is printed in the Appendix (A-1).[1]

[1] The designation "(A)" refers to the Appendix hereto and the designation "(R)" refers to the Appendix Accompanying Opening Brief for Petitioner in the Court of Appeals.

Statement of Jurisdiction.

The judgment of the Court of Appeals was entered on January 13, 1960, and the jurisdiction of this Court is invoked under 62 Stat. 928 (1948), 28 U. S. C. §1254(1) (1958).

Questions Presented.

1. Does the dismissal of the petition to review the decision of the Tax Court for lack of jurisdiction by the Court of Appeals conflict with decisions of the Courts of Appeals for the Sixth, Eighth and Ninth Circuits in *Dowd-Feder, Inc.* v. *Commissioner*, 173 F. 2d 673 (6th Cir. 1949), *Dayton Rubber Co.* v. *Commissioner*, 249 F. 2d 2 (6th Cir. 1957), *Packer Pub. Co.* v. *Commissioner*, 211 F. 2d 612 (8th Cir. 1954), and *Stimson Mill Co.* v. *Commissioner*, 163 F. 2d 269 (9th Cir. 1947), *cert. denied*, 332 U. S. 824 (1947), *reh. denied*, 332 U. S. 839 (1947)?

2. Is the Court of Appeals deprived by Section 732(c) of the Internal Revenue Code of 1939 of jurisdiction to review a decision of the Tax Court holding that the "growth formula" of Section 742(h) may not be employed together with Section 722 in a case where the amount of relief, if any, under Section 722 has been stipulated?

Statutes Involved.

The controlling statute is Section 732(c) of the Internal Revenue Code of 1939, 55 Stat. 26 (1941), which provides:

> "(c) Finality of Determination.—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711(b)(1)(H), (I), (J), or (K),

section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Board."

Also involved here are Sections 713, 722 and 742 of the Internal Revenue Code of 1939, the relevant portions of which are printed in the Appendix (A-8-11).[2]

Statement of the Case.

This petition involves the jurisdiction of the several Courts of Appeals to review decisions of the Tax Court, and presents the question of when the determination of a question is "necessary solely by reason of * * * section 722" within the meaning of Section 732(c). A brief statement of the operation of the Second World War Excess Profits Tax as it applies to this case is necessary to frame the jurisdictional issue.

The excess profits tax appearing in Subchapter E of Chapter 2 of the Internal Revenue Code of 1939 is an extremely complicated piece of legislation designed to accomplish a readily understandable objective. That objective was to provide funds during a period of national emergency by subjecting to a high rate of taxation earnings attributable to the wartime economy, *i.e.*, earnings realized during the years 1940 through 1945 in excess of normal or peacetime earnings. *Commissioner* v. *South Texas Co.*, 333 U. S. 496 (1948); *United States* v. *Koppers Co.*, 348 U. S. 254 (1955). The complexity of the statute arises primarily from the mechanics adopted by Congress to segregate excessive earnings, not all the details of which are important here.

---

[2] Sections of the Internal Revenue Code of 1939 will hereinafter be designated "Section ".

One method provided by Congress for determining the extent to which profits during the wartime years were excessive is to compare those profits with what is called the "average base period net income" (usually abbreviated ABPNI). This ABPNI is a measure of what Congress deemed to be normal or peacetime earnings, and is based upon the taxpayer's average earnings during the four "base period" years 1936 through 1939. In general, profits in excess of 95% of the ABPNI are deemed to be excessive and are subjected to the excess profits tax. Section 713(a) (A-8).

So far as is relevant here, three methods are provided by which the ABPNI may be computed. In the usual case the ABPNI is simply the arithmetic average of the annual earnings realized by the taxpayer during the base period years. Section 713(e) (A-8, 9). In addition, however, two formulae are provided for calculating the ABPNI, one known as the "75% rule" (Sections 713(e) and 742(b)(2)) and the other as the "growth formula" (Sections 713(f) and 742(h) (A-9, 11)).

The 75% rule is applicable where earnings in one base period year are less than 75% of the average earnings in the other three base period years. When this is so, the statute provides that 75% of the average earnings in the other three base period years shall be substituted for the earnings in the lowest base period year in computing the ABPNI. This rule results in an ABPNI greater than the arithmetic average and so compensates for unusually low earnings in a single base period year.

In calculating the ABPNI in cases where earnings in the last two base period years (1938 and 1939) exceeded earnings in the first two (1936 and 1937), the "growth formula" must be used. Under the growth formula one half of such excess is added to the average earnings in the

last two base period years, which are then the only years used in determining the ABPNI. This device also results in an ABPNI greater than the arithmetic average of actual earnings during the base period, and thus compensates for the fact that the taxpayer's earnings were increasing (presumably due to non-wartime causes) as the wartime years approached. The petitioner herein calculated its ABPNI under the growth formula of Section 742(h), and the respondent does not question its right to do so.

In adopting the plan of taxation described above, Congress realized that there would be cases where calculation of an ABPNI under one of the three methods described above resulted in an inadequate standard of normal or peacetime earnings, and Section 722 was enacted to meet this problem. That section provides that where the taxpayer can establish (1) that the tax without the benefit of Section 722 is "excessive and discriminatory" and (2) what would be "a fair and just amount representing normal earnings", then such amount is to be used as a "constructive average base period net income" (usually abbreviated CABPNI) in lieu of the ABPNI otherwise determined. Section 722(a) (A-10). Section 722 goes on to list certain instances in which the tax computed without its benefit "shall be considered to be excessive and discriminatory", among which is the case where during the base period years a taxpayer "changed the character of the business and the average base period net income does not reflect the normal operation for the entire base period of the business." Section 722(b)(4) (A-10, 11).

The petitioner in this case claimed relief under Section 722(b)(4) on two grounds, each of which the respondent conceded qualifies as a change in the character of its business under Section 722(b)(4). These changes were (1) the acquisition by petitioner on the last business day of the

base period of all the assets of a competitor, Fisk Rubber Company, and (2) a change in the ratio of nonborrowed capital to total capital during the base period. In addition, the petitioner and respondent stipulated in the Tax Court "appropriate adjustments" under Section 722 on account of these two factors (R 15a). The sum of these stipulated amounts represents the increase in the petitioner's ABPNI, if any, to be made in arriving at a CABPNI, and the sole issue presented to the Tax Court was the figure to which these stipulated adjustments should be added.

It was the position of the petitioner before the Tax Court that it was entitled to the benefits afforded it by the growth formula of Section 742(h) and that the stipulated Section 722 adjustments should be added to that figure. The respondent, on the other hand, maintained that petitioner was not entitled to the benefits of both the growth formula of Section 742(h) and the stipulated adjustments under Section 722, and that the Section 722 adjustments could be added only to the arithmetic average of the petitioner's base period earnings in computing the allowable relief. The Tax Court, sustaining the respondent, held that "the method provided in Section 722 may not be combined with the method allowed by Section 742(h)", and denied relief (R 6a).

The petitioner petitioned the Court of Appeals pursuant to 68A Stat. 890 (1954), 26 U. S. C. §7482(a) (1958), to review the decision of the Tax Court, claiming on appeal that the effect of the Tax Court decision was to force the petitioner to give up either the benefit of the growth formula of Section 742(h), to which Congress has declared it entitled, or the benefit of the Section 722 adjustments, which the respondent has stipulated are appropriate. The Court of Appeals dismissed the petition for review on the ground that the decision of the Tax Court was a deter ina-

tion of a question made necessary "solely by reason of" Section 722 within the meaning of Section 732(c)(A-5).

In refusing to accept jurisdiction in the present case the Court of Appeals construed the word "solely" in Section 732(c) so as to preclude judicial review of all Tax Court decisions where Section 722 is involved whether or not the question to be determined turns upon other statutory provisions as well. The decision of the Court of Appeals herein interprets "solely by reason of" to mean "partly by reason of" and thereby deprives petitioner of any judicial review. As shown below, such an interpretation is contrary to decisions of other Courts of Appeals and to the intention of Congress in enacting Section 732(c).

Reasons for Allowance of the Writ.

The Decision of the Court of Appeals Conflicts with Decisions of the Courts of Appeals for the Sixth, Eighth and Ninth Circuits.

The Courts of Appeals for the Sixth, Eighth and Ninth Circuits have assumed jurisdiction to review decisions of the Tax Court in cases directly in point with the present case, holding that Section 732(c) did not prohibit such review.

In *Stimson Mill Co.* v. *Commissioner,* 163 F. 2d 269 (9th Cir. 1947), the taxpayer was entitled to increase its 1938 earnings under the 75%-rule, materially increasing its ABPNI, and the parties stipulated an appropriate amount of relief under Section 722 because of a strike in 1937. The issue presented to the Tax Court was whether the taxpayer was entitled to substitute the increased Section 722 figure for 1937 and then apply the 75% rule to raise its 1938 earnings. The Court of Appeals, upholding its jurisdiction to

review the Tax Court's decision over challenge by the Commissioner under Section 732(c), stated:

> "We think the determination of the question before the Tax Court involved both §722 and §713(e)(1) [the 75% rule].
>
> It is of course possible to cast the problem, as the Government has done, solely in terms of §722 by stating that taxpayer was allowed the benefits of [the 75% rule] and that the only question is whether he is entitled to §722 relief. But the nature of the §722 relief sought by taxpayer should not be overlooked. * * *.
>
> Taxpayer asks to raise both 1937 and 1938 earnings by the use of both sections. It was this double relief that the Government refused to allow, and the determination of that question clearly was necessary by reason of both sections. For were it not for [the 75% rule] taxpayer could have no question as to his tax liability to be determined."

To precisely the same extent that the 75% rule was involved in *Stimson Mill Co.* the growth formula is involved in the present case. Here, were it not for the growth formula of Section 742(h), there could be no question as to the petitioner's excess profits tax liability, and the dismissal of the petition for review in this case is directly in conflict with the decision of the Court of Appeals for the Ninth Circuit.

In *Dowd-Feder, Inc.* v. *Commissioner*, 173 F. 2d 673 (6th Cir. 1949), a Section 722 adjustment increasing the taxpayer's earnings for 1939 was stipulated, and the issue presented was whether the taxpayer was entitled to that relief and also to the benefit of the 75% rule. On appeal from the Tax Court, the Court of Appeals upheld its juris-

diction to review, following *Stimson Mill Co.*, on the ground that both the 75% rule and Section 722 were involved.[3]

This interpretation of Section 732(c) was confirmed by the same Court in *Dayton Rubber Co.* v. *Commissioner*, 249 F. 2d 2 (6th Cir. 1957), where the Court of Appeals assumed jurisdiction to review a decision of the Tax Court holding that the taxpayer was not entitled to the benefits of both the growth formula and a stipulated adjustment under Section 722 (the same issue presented here). These decisions of the Court of Appeals for the Sixth Circuit cannot be reconciled with the decision below in this case.

In *Packer Pub. Co.* v. *Commissioner*, 211 F. 2d 612 (8th Cir. 1954), the Commissioner had granted relief under Section 711(b)(1)(J) (thus eliminating certain abnormal deductions during the base period). The taxpayer then applied for relief under Section 722, and the Tax Court held that in computing the Section 722 CABPNI no consideration could be given to the Section 711(b) relief previously granted. As the Court of Appeals for the Eighth Circuit noted, the Tax Court was correct only "if relief under §722 necessarily and automatically excluded any relief under §711". In upholding its jurisdiction to review the Tax Court decision over challenge under Section 732(c) by the Commissioner, the Court of Appeals held that "[s]uch a decision of the Tax Court is not within the purview of the prohibition of §732(c)."

In the present case the Tax Court was correct only if relief under Section 722 "necessarily and automatically

[3] It should be noted that in an earlier case denying jurisdiction under Section 732(c) the Court of Appeals for the Second Circuit stated: "The case of Dowd-Feder *v.* Commissioner, * * * relied upon by the petitioner, is not to the contrary, since there the decision of the Tax Court did not depend solely upon section 722." *George Kemp Real Estate Co.* v. *Commissioner*, 182 F. 2d 847, 849 (2d Cir. 1950), *cert. denied*, 340 U. S. 852 (1950).

excluded any relief under" Section 742(h) (the growth formula), and the decision of the Court of Appeals herein conflicts with the decision of the Court of Appeals for the Eighth Circuit in *Packer Pub. Co.*

In its opinion in this case the Court of Appeals quotes from the respondent's brief stating that the issue presented is "whether the taxpayer was entitled to *both* relief under Section 722 *and* the benefit of the 'growth formula' computation under Section 742(h)." Nevertheless, speaking of petitioner's reliance on *Stimson Mill Co.* and *Dowd-Feder, Inc.* on the jurisdictional question, the Court of Appeals stated:

> "We think that in each of these cases, as in this, only a §722 question was involved, *i. e.*, the proper computation of the taxpayer's CABPNI under §722, *and with deference we cannot accept the analysis of the problem made in those opinions.*"[4] (Emphasis supplied.)

It is evident from its opinion that the Court of Appeals recognized the existing conflict among the Courts of Appeals as to the meaning of Section 732(c).

The Importance of the Federal Jurisdictional Question Presented.

The question of the scope of judicial review available to taxpayers under a statute imposing a tax at rates of 80% or more is of obvious importance. Surely the petitioner,

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[4] The Court of Appeals went on to suggest that "the *Stimson Mill* case may no longer control in the Ninth Circuit; it appears to have been overruled, *sub silentio*, by *Helms Bakeries* v. *Commissioner of Int. Rev., supra.* And the Court in the Sixth Circuit in its *Dowd-Feder* decision relied upon *Stimson Mill.*" The petitioner finds no inference in the *Helms Bakeries* opinion (263 F. 2d 642) that *Stimson Mill Co.* is overruled since *Helms Bakeries* in the view of the Ninth Circuit apparently involved only the question of the relief sought under Section 722.

having paid more than $80,000,000 in excess profits taxes from 1940 through 1945, is entitled to judicial review with regard to the portion of those taxes (approximately 2%) which in its opinion represented a tax not on excess profits but on its normal profits. Moreover, the question presented here goes far beyond the facts of this case since on March 23, 1960 there were 83 cases docketed in the Tax Court involving Sections 721 and 722 in which the interpretation of Section 732(c) may determine whether or not any judicial review of the decision of the Tax Court will be available.[5]

The provisions of the law with respect to which Section 732(c) denies review are portions of Section 711 (relating to abnormal deductions during the base period years), Section 721 (relating to abnormal income during the wartime or excess profits tax years) and Section 722 (the general relief provision involved here). These sections comprise the so-called "abnormality" or "hardship" provisions, and in connection with the review available under certain of these sections the Senate Committee on Finance has stated:

> "Because of the complicated nature and the economic character of the issues involving relief under section 722 * * * it is essential that all such issues be decided by one group familiar with the problems involved." S. Rep. No. 1631, 77th Cong., 2d Sess., pp. 206, 207 (1942). See also H. R. Rep. No. 2333, 77th Cong., 2d Sess., p. 149 (1942).

Certainly the wisdom of Congress in sparing the Courts of Appeals from the burden of the involved economic analysis inherent in the abnormality provisions of the excess profits tax is beyond question. However, the intent

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[5] The above information as to the number of docketed cases was furnished to the petitioner by letter dated March 23, 1960 from the Administrative Officer of the Tax Court.

of Congress in enacting Section 732(c) should not be extended to prohibit judicial review of cases involving no such analysis. In the present case the amount of relief appropriate under Section 722(b)(4) was stipulated, and the question presented to the Tax Court turned primarily on the applicability of the growth formula of Section 742(h), the result of which was also stipulated. To apply the prohibition of Section 732(c) in this case is in no sense justified by the purpose of that section.

Moreover, the interpretation of the word "solely" in Section 732(c) by the Court of Appeals cannot be reconciled with the common meaning of that word or with its interpretation by this Court. As Mr. Justice Douglas stated in interpreting a Federal income tax provision, "'Solely' leaves no leeway", *Helvering* v. *Southwest Corp.*, 315 U. S. 194, 198 (1942), and this is particularly true where, as in the present case, the result of a contrary interpretation is to deprive a taxpayer of judicial review.

Review by an appellate court should never be denied unless the statute clearly requires such a result. As the Treasury Department stated when it placed itself on record as favoring the repeal of Section 732(c):

> " 'in any legal issue which is presented to any legal tribunal in our system of government there should be an appeal on a legal question to an appellate court.' " H. R. Rep. No. 1370, 83d Cong., 2d Sess., p. 8 (1954).

In *Stern & Stern Textiles, Inc.* v. *Commissioner*, 262 F. 2d 538 (2d Cir. 1959), *cert. denied*, October 12, 1959, the Court of Appeals for the Second Circuit assumed jurisdiction to review a Tax Court decision denying the taxpayer the right to litigate a claim for relief under Section

722(b). In discussing its decision to accept jurisdiction the Court stated:

> "If, as the Commissioner asserts, decisions in other circuits are in conflict with it, an authoritative ruling can probably be obtained by certiorari."

The need for such a ruling is imperative.

Conclusion.

In summary, this case presents a decision by the Court of Appeals that is contrary to the clear intent of Congress and is in conflict with decisions of other Courts of Appeals as to the breadth of the limitation on Federal appellate jurisdiction of Section 732(c). Under these circumstances the obvious importance of the questions presented herein calls for an exercise of this Court's power of supervision.

Respectfully submitted,

D. Nelson Adams,
Counsel for Petitioner,
15 Broad Street,
New York 5, N. Y.

John A. Reed,

Richard R. Dailey.

APPENDIX.

Opinion of the Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT.

No. 3—October Term, 1959.

(Argued November 4, 1959—Decided January 13, 1960.)

Docket No. 25322.

UNITED STATES RUBBER COMPANY,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Before:

CLARK, HINCKS and WATERMAN,
Circuit Judges.

Petition by taxpayer to review decision of the Tax Court, Murdock, J., 29 T. C. 1268, sustaining the Commissioner's finding that no refund of excess profits taxes is due petitioner for the years 1941 through 1945 under the provisions of Section 722, Internal Revenue Code of 1939. Petition dismissed for lack of jurisdiction to review. Section 732(c) of the Code of 1939.

MONTGOMERY B. ANGELL, New York, N. Y. (John A. Reed and Richard R. Dailey, New York, N. Y., on the brief), for Petitioner.

HARRY MARSELLI, Atty., Dept. of Justice, Washington, D. C. (Charles K. Rice, Asst. Atty. General, and Meyer Rothwacks, Atty., Dept. of Justice, Washington, D. C., on the brief), for Respondent.

HINCKS, Circuit Judge:

Review is sought of a decision of the Tax Court [29 T. C. 1268] which upheld the Commissioner's denial of petitioner's application for excess profits tax relief for the years 1941 through 1945 under §722 of the 1939 Code, 26 U. S. C. A. Excess Profits Taxes, §722,[1] the section for relief as to so-called abnormalities. Not only have the parties stipulated that during the base period two changes occurred in the character of the petitioner's business, as that phrase

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[1] "§722. *General relief—Constructive average base period net income*

"(a) *General rule.* In any case in which the taxpayer establishes that the tax computed under this subchapter (without the benefit of this section) results in an excessive and discriminatory tax and establishes what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon a comparison of normal earnings and earnings during an excess profits tax period, the tax shall be determined by using such constructive average base period net income in lieu of the average base period net income otherwise determined under this subchapter. In determining such constructive average base period net income, no regard shall be had to events or conditions affecting the taxpayer, the industry of which it is a member, or taxpayers generally occurring or existing after December 31, 1939, except that, in the cases described in the last sentence of section 722(b)(4) and in section 722(c), regard shall be had to the change in the character of the business under section 722(b)(4) or the nature of the taxpayer and the character of its business under section 722(c) to the extent necessary to establish the normal earnings to be used as the constructive average base period net income.

"(b) *Taxpayers using average earnings method.* The tax computed under this subchapter (without the benefit of this section) shall be considered to be excessive and discriminatory in the case of a taxpayer entitled to use the excess profits credit based on income pursuant to section 713, if its average base period net income is an inadequate standard of normal earnings because—

* * * * * *

"(4) the taxpayer, either during or immediately prior to the base period, commenced business or changed the character of the business and the average base period net income does not reflect the normal operation for the entire base period of the business. If the business of the taxpayer did not reach, by the end of the base period, the earning level which it would have reached if the taxpayer had commenced business or made the change in the character of the business two years before it did so, it shall be deemed to have commenced the business or made the change at such earlier time. For the purposes of this subparagraph, the term 'change in the character of the business' includes a change in the operation or management of the business, a difference in the products or services furnished, a difference in the capacity for production or operation, a difference in the ratio of nonborrowed capital to total capital, and the acquisition before January 1, 1940, of all or part of the assets of a competitor, with the result that the competition of such competitor was eliminated or diminished. * * *"

is defined in §722(b)(4), but also they agreed as to the appropriate adjustments resulting from such changes, and as to the fact that such adjustments would not duplicate any of the petitioner's earnings included in its average base period net income (ABPNI), as computed under §742(h). The Tax Court, drawing upon the language of §722, accordingly framed two issues for decision, viz., "whether the petitioner has shown that its average base period net income, without the benefit of section 722, is an inadequate standard of its normal earnings because of the admitted change in the character of its business * * *" and "whether it has established what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income (CABPNI) 'in lieu of the average base period net income otherwise determined under this subchapter' in computing the excess profits credit based on income." The issues thus posed were both decided adversely to petitioner.

At the threshold we are met with the Commissioner's contention that, by reason of §732(c), we are without jurisdiction to review the determination below because it was of questions made "necessary solely by reason of * * * section 722."[2] We proceed, therefore, to a consideration of this jurisdictional problem.

As shown above, the Tax Court stated that the only issues involved were the establishment by the taxpayer of two conditions upon which relief under §722 depended.

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[2] "§732. *Review of abnormalities by Tax Court of the United States*

"(c) *Finality of determination.* If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of * * * section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Tax Court.

* * * * * * *

"(d) *Review by special division of the Tax Court.* The determinations * * * by any division of the Tax Court involving any question arising under * * * section 722 * * * shall be reviewed by a special division of the Tax Court which shall be constituted by the presiding judge and consist of not less than three judges of the Tax Court. The decisions of such special division shall not be reviewable by the Tax Court, and shall be deemed decisions of the Tax Court."

The procedure of §732(d) was followed in the instant case.

The Commissioner in his brief defined the question presented as follows:

> "The broad issue in this case is whether the taxpayer was entitled to relief under Section 722 of the 1939 Internal Revenue Code, where a proper reconstruction of its base period income for the items qualifying as grounds for relief under Section 722 resulted in an amount which was less than its average base period net income computed (without the benefit of Section 722) under Section 742(h) of that Code.
>
> "More specifically, the question presented is whether, in arriving at its 'constructive average base period net income' under Section 722(a), the taxpayer was also entitled to the benefits of the so-called 'growth formula' used in computing its 'average base period net income' under Section 742(h)—*i. e.*, whether the taxpayer was entitled to *both* relief under Section 722 *and* the benefits of the 'growth formula' computation under Section 742(h)."

The taxpayer in its reply brief defines the issue as follows:

> "• • • The issue, more accurately stated, is whether in determining the amount of the credit, petitioner is entitled to a 'constructive average base period net income' under Section 722(a) computed by the sum of the Section 742(h) formula applied only to its own actual base period earnings and one or both of the two unrelated stipulated reconstructions under Section 722(b)(4), and to use such 'constructive average' in place of the base period average otherwise determined, when the two sets of computations are entirely independent, one from the other."

It thus appears plain that in each of these three definitions of the issues it is recognized that the only problem involves a determination of the proper "constructive average base period net income" under §722(a).

Moreover, our own independent analysis of the issues, in the light of the stipulation in the Tax Court and the findings in the thoughtful opinion of Judge Murdock, convinces us that the determination sought was one made "necessary solely by reason of • • • section 722." It will be noted that there is no dispute between the parties as to the existence and amount of any "change in the character of the business" of the taxpayer under §722(b)(4), and no dispute that such changes as occurred were properly reflected in the Commissioner's computation of the taxpayer's CABPNI: Nor is there any dispute as to the amount of the excess income tax credit under the "growth formula" of §742(h). And the Commissioner gave the taxpayer the full benefit of this credit. The only question is one of method in determining the CABPNI under §722(a), i.e., whether for purposes of determining the excess profits credit petitioner's CABPNI may properly reflect the Supplement A ABPNI computed under §742(h) in addition to the credits for "changes in character of the business" authorized by §722(b)(4). We cannot escape the conclusion that the only determination involved is one "necessary solely by reason of • • • section 722." Consequently, we hold that under §732(c) we are without jurisdiction to review.

Our conclusion is in accord with *Helms Bakeries* v. *Commissioner of Int. Rev.*, 9 Cir., 236 F. 2d 3, 263 F. 2d 642, cert. denied 360 U. S. 903; *Colorado Milling & El. Co.* v. *Commissioner of Int. Rev.*, 10 Cir., 205 F. 2d 551; cf. *Brown Paper Mill Co.* v. *Commissioner of Int. Rev.*, 5 Cir., 255 F. 2d 77, cert. denied 358 U. S. 906. It is not in conflict with our decisions in *George Kemp Real Estate Co.* v. *Commissioner of Int. Rev.*, 2 Cir., 205 F. 2d 236; *Stern & Stern Textiles, Inc.* v. *Commissioner of Int. Rev.*, 263 F. 2d 538; *Headline Publications, Inc.* v. *Commissioner of Int. Rev.*, 2 Cir., 263 F. 2d 541. We reviewed on the merits in the former two cases because the Tax Court's decisions were based upon the doctrine of collateral estoppel and not upon §722 as was its decision in the case now before us, and in

the latter case because the only contested issue which had been submitted to the Tax Court was a question as to the statute of limitations.

The petitioner relies on *Dowd-Feder* v. *Commissioner of Int. Rev.*, 6 Cir., 173 F. 2d 673, and *Stimson Mill Co.* v. *Commissioner of Int. Rev.*, 9 Cir., 163 F. 2d 269, cert. denied 332 U. S. 824, reh. denied 332 U. S. 839, affirming 7 T. C. 1065, in both of which cases jurisdiction was sustained over challenge by the Commissioner. We think that in each of these cases, as in this, only a §722 question was involved, i.e., the proper computation of the taxpayer's CABPNI under §722, and with deference we cannot accept the analysis of the problem made in those opinions. We suggest that the *Stimson Mill* case may no longer control in the Ninth Circuit: it appears to have been overruled, *sub silentio*, by *Helms Bakeries* v. *Commissioner of Int. Rev.*, *supra*. And the Court in the Sixth Circuit in its *Dowd-Feder* decision relied upon *Stimson Mill*.

Petition dismissed.

Judgment of the Court of Appeals.

UNITED STATES COURT OF APPEALS,

SECOND CIRCUIT.

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the thirteenth day of January one thousand nine hundred and sixty.

Present:

Hon. CHARLES E. CLARK,
Hon. CARROLL C. HINCKS,
Hon. STERRY R. WATERMAN,
Circuit Judges.

UNITED STATES RUBBER CO.,
Petitioner on Review,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

APPEALS FROM THE TAX COURT OF THE UNITED STATES.

This cause came on to be heard on the transcript of record from The Tax Court of the United States, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the petition from the order of said The Tax Court of the United States be and it hereby is dismissed.

A. DANIEL FUSARO,
Clerk.

Statutes Involved.

Internal Revenue Code of 1939.

Sec. 713. Excess Profits Credit—Based on Income.

(a) *Amount of Excess Profits Credit.*—The excess profits credit for any taxable year, computed under this section, shall be—

(1) Domestic corporations.—In the case of a domestic corporation-

(A) 95 per centum of the average base period net income.

(B) Plus 8 per centum of the net capital addition as defined in subsection (g), or

(C) Minus 6 per centum of the net capital reduction as defined in subsection (g).

* * * * * * *

(e) *Average Base Period Net Income—General Average.*—The average base period net income determined under this subsection shall be determined as follows:

(1) By computing the aggregate of the excess profits net income for each of the taxable years of the taxpayer in the base period, reduced by the sum of the deficits in excess profits net income for each of such years. If the excess profits net income (or deficit in excess profits net income) for one taxable year in the base period divided by the number of months in such taxable year is less than 75 per centum of the aggregate of the excess profits net income (reduced by deficits in excess profits net income) for the other taxable years in the taxpayer's base period divided by the number of months in such other taxable years (herein called "average monthly amount") the amount used for such one year under this paragraph shall be 75 per centum of the average monthly amount multiplied by the number of months in such one year, and the year increased under this sentence shall be the year the increase in which will produce the highest average base period net income;

(2) By dividing the amount ascertained under paragraph (1) by the total number of months in all such taxable years; and

(3) By multiplying the amount ascertained under paragraph (2) by twelve.

(f) *Average Base Period Net Income—Increased Earnings in Last Half of Base Period.*—The average base period net income determined under this subsection shall be determined as follows:

(1) By computing, for each of the taxable years of the taxpayer in its base period, the excess profits net income for such year, or the deficit in excess profits net income for such year;

(2) By computing for each half of the base period the aggregate of the excess profits net income for each of the taxable years in such half, reduced, if for one or more of such years there was a deficit in excess profits net income, by the sum of such deficits. For the purposes of such computation, if any taxable year is partly within each half of the base period there shall be allocated to the first half an amount of the excess profits net income or deficit in excess profits net income, as the case may be, for such taxable year, which bears the same ratio thereto as the number of months falling within such half bears to the entire number of months in such taxable year; and the remainder shall be allocated to the second half;

(3) If the amount ascertained under paragraph (2) for the second half is greater than the amount ascertained for the first half, by dividing the difference by two;

(4) By adding the amount ascertained under paragraph (3) to the amount ascertained under paragraph (2) for the second half of the base period;

(5) By dividing the amount found under paragraph (4) by the number of months in the second half of the base period and by multiplying the result by twelve;

(6) The amount ascertained under paragraph (5) shall be the average base period net income determined under this subsection, except that the average base period net income determined under this subsection shall in no case be greater than the highest excess profits net income for any taxable year in the base period. • • •

Sec. 722. General Relief—Constructive Average Base Period Net Income.

(a) *General Rule.*—In any case in which the taxpayer establishes that the tax computed under this subchapter (without the benefit of this section) results in an excessive and discriminatory tax and establishes what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon a comparison of normal earnings and earnings during an excess profits tax period, the tax shall be determined by using such constructive average base period net income in lieu of the average base period net income otherwise determined under this subchapter.

• • •

(b) *Taxpayer's Using Average Earnings Method.*—The tax computed under this subchapter (without the benefit of this section) shall be considered to be excessive and discriminatory in the case of a taxpayer entitled to use the excess profits credit based on income pursuant to section 713, if its average base period net income is an inadequate standard of normal earnings because—

• • •

(4) the taxpayer, either during or immediately prior to the base period, commenced business or changed the character of the business and the average base period net income does not reflect the normal operation for the entire base period of the business. • • • For the purposes of this subparagraph, the term "change in the character of the

business" includes a change in the operation or management of the business, a difference in the products or services furnished, a difference in the capacity for production or operation, a difference in the ratio of non-borrowed capital to total capital, and the acquisition before January 1, 1940, of all or part of the assets of a competitor, with the result that the competition of such competitor was eliminated or diminished.

Sec. 742. Supplemental A Average Base Period Net Income.

In the case of a taxpayer which is an acquiring corporation, its average base period net income (for the purpose of the credit computed under section 713) shall be the amount computed under section 713 or the amount of its Supplement A average base period net income, whichever is the greater. The Supplement A average base period net income shall be the amount computed without regard to subsection (h) of this section or computed under subsection (h) of this section, whichever is the greater. The Supplement A average base period net income shall be computed as follows:

(h). *Increased earnings in last half of Base Period—*

(1) *General rule.*—The Supplement A average base period net income determined under this subsection shall be computed by ascertaining for each half of the base period the sum of the plus amounts determined under subsection (a) reduced if for any year in such half a minus amount was determined by the minus amount of such year. If the amount ascertained for the second half exceeds the amount ascertained for the first half, the Supplement A average base period net income shall be the sum, divided by two, of the amount so ascertained for the second half plus one-half of such excess, except that it shall not exceed the largest plus amount determined under subsection (a) with respect to any base period year.

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No. 842

In the Supreme Court of the United States

OCTOBER TERM, 1959

UNITED STATES RUBBER COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

J. LEE RANKIN,
Solicitor General,
CHARLES K. RICE,
Assistant Attorney General,
LEE A. JACKSON,
HARRY MARSELLI,
Attorneys,
Department of Justice, Washington 25, D.C.

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UNITED STATES RUBBER COMPANY, PETITIONER

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Tax Court (P.A. 2a–11a)[1] is reported at 29 T.C. 1268. The opinion of the Court of Appeals (Pet. A–1—A–6) is reported at 274 F. 2d 307.

JURISDICTION

The judgment of the Court of Appeals was entered on January 13, 1960. (Pet. A–7.) The petition for a writ of certiorari was filed on April 8, 1960. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

[1] "P.A." refers to petitioner's appendix in the court of appeals; "R.A." to respondent's.

QUESTION PRESENTED

Whether the Tax Court's denial of relief under Section 722 of the 1939 Internal Revenue Code may—notwithstanding the provision of Section 732(c) that the Tax Court's determination of any question "necessary solely by reason of * * * section 722 * * * shall not be reviewed or redetermined by any court"—be reviewed with respect to the proper method of reconstruction of base period earnings under Section 722, or, more specifically, with respect to the taxpayer's contention that in arriving at its "constructive average base period net income" under Section 722(a) it was also entitled to the benefit of the so-called "growth formula" of Section 742(h), in addition to the appropriate adjustments for the items concededly qualifying for relief under Section 722 (b)(4).

STATUTE INVOLVED

The provisions of Section 732 of the 1939 Internal Revenue Code are set forth in the Appendix, *infra*, pp. 15–16, together with the pertinent portions of Sections 713, 722, 740 and 742 (pp. 10–15, 16–19).

STATEMENT

The taxpayer petitioned the Tax Court for redetermination of the Commissioner's disallowance of its applications for relief under Section 722 as to its excess profits taxes[1] for the years 1941 through 1945 (R.A. 93–98).

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[1] Briefly, under the Second World War excess profits tax law, Section 710, *et seq.*, of the 1939 Code, a tax was imposed upon corporate profits in excess of a certain level or norm, called the "excess profits credit", deemed to represent the taxpayer's

In the Tax Court, the parties stipulated all of the facts and left for decision, in effect, only a narrow question as to the proper reconstruction of base period earnings under Section 722. (P.A. 2a–7a, 12a–27a; R.A. 98–101, Ex. 10–J following p. 101.) Taking the figures applicable to the taxable years 1943 through 1945 as illustrative, the arithmetic average of the taxpayer's actual base period earnings was $13,548,117.26. (P.A. 24a–25a.) The parties stipulated that there were two changes in the character of the taxpayer's business during the base period within the meaning of Section 722(b)(4), by reason of the taxpayer's acquisition of the assets of a competitor and by reason of a change in ratio of nonborrowed capital to total

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"normal" profits. The credit, computed under Section 713 (or its counterpart applicable to taxpayers having qualifying subsidiaries, Section 742) was based on the taxpayer's (and its subsidiaries') average earnings during the "base period," 1936–1939. In determining the "average base period net income" on that method, two alternative automatic adjustments were provided: (1) under the "75% rule", the earnings of any year in the base period could be increased to 75% of the average for the other years (Sections 713(e) and 742(b)(2)); (2) under the "growth formula", an increased credit was allowed if the earnings for the last half of the base period were greater than those for the first half (Sections 713(f) and 742(h)).

In lieu of those automatic computation adjustments or benefits, the law further permitted "general relief"—in the case of a number of enumerated "abnormalities" or conditions—under Section 722 upon the basis of a *reconstruction* of base period earnings (specifically, upon the basis of a "constructive average base period net income", to be used "in lieu of the average base period net income otherwise determined"), if the taxpayer could establish that its base period income was not normal for any of the reasons specified in the statute and if it could establish "what would be a fair and just amount representing normal earnings." Section 722(a), Appendix, *infra*, p. 13.

capital, and that the respective amounts of $618,016.75 and $306,719.75 (aggregating $924,736.50) constituted appropriate adjustments (in arithmetic averages, for the four base period years) for those two changes in character. (P.A. 9a, 15a, 24a.) Adding the $924,736.50 aggregate adjustments for those changes to the $13,548,117.26 arithmetic average of the taxpayer's actual base period earnings would result in reconstructed average earnings of $14,472,853.76. (P.A. 9a, 24a.) By the application of the "growth formula" of Section 742(h) to the taxpayer's actual base period earnings, the "average base period net income" (or ABPNI) became $15,383,336.90.[3] (P.A. 24a–25a.)

The taxpayer contended, in substance, that, in arriving at its "constructive average base period net income" (or CABPNI) under Section 722(a), it was entitled to begin with the "growth formula" $15,383,336.90 amount of its ABPNI as computed under Section 742(h) and to add thereto the $924,736.50 aggregate adjustments (in arithmetic averages) stipulated as appropriate for the two Section 722(b)(4) grounds. (P.A. 5a–7a, 16a–17a.) The Commissioner's position was that the $924,736.50 aggregate for the two stipulated adjustments should be added only to the $13,548,117.26 average of the actual base period earnings and that, since that resulting amount ($14,472,853.76) was less than the $15,383,336.90 arrived at

[3] The taxpayer had been allowed a credit based upon the latter figure by the Commissioner, and the Tax Court did not disturb that allowance. (See R.A. 99–100 and Ex. 10 J following p. 101; P.A. 2a, 5a, 6a, 11a; Pet. A–5.)

under the "growth formula", the taxpayer was not entitled to any relief under Section 722. (P.A. 15a–16a, 24a.)

The Tax Court sustained the Commissioner's position, and denied the taxpayer any relief under Section 722 on the ground that a proper reconstruction of base period earnings under Section 722 resulted in an amount which was less than the amount already allowed to the taxpayer under the "growth formula" of Section 742(h). (P.A. 5a–11a.)[4] The Court of Appeals, taking the view that the question presented related solely to the proper method of reconstruction of base period earnings under Section 722, dismissed the petition for review, in observance of Section 732 (c). (Pet. A–2—A–6, A–7.)

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[4] The Tax Court's holding was, we believe, clearly correct under the explicit provision of Section 722(a) that a CABPNI under Section 722 may be used only "in lieu of the average base period net income otherwise determined" under the excess profits tax subchapter. The Tax Court thus followed the principle, adhered to in a long line of decisions, to the effect that a taxpayer may not avail itself of both relief under Section 722 and the benefits of one of the automatic computation adjustments under Section 713 (or their counterparts under Section 742). See *Stimson Mill Co.* v. *Commissioner*, 7 T.C. 1065, affirmed, 163 F. 2d 269 (C.A. 9th), certiorari denied, 332 U.S. 824; *Homer Laughlin China Co.* v. *Commissioner*, 7 T.C. 1325; *Dowd-Feder, Inc.* v. *Commissioner*, 10 T.C. 345, affirmed, 173 F. 2d 673 (C.A. 6th); *Acme Breweries* v. *Commissioner*, 15 T.C. 682; *Dayton Rubber Co.* v. *Commissioner*, 26 T.C. 389, affirmed, 249 F. 2d 2 (C.A. 6th); *Central Bag Co.* v. *Commissioner*, 27 T.C. 230; *Clayton Coal Co.* v. *Commissioner*, 27 T.C. 810. See also *Helms Bakeries* v. *Commissioner*, 23 T.C. 967, 986–987, remanded on another ground, 236 F. 2d 3 (C.A. 9th); *Brown Paper Mill Co.* v. *Commissioner*, 23 T.C. 47, 63, review dismissed, 255 F. 2d 77, certiorari denied, 358 U.S. 906; *Atlas Foundry Co.* v. *Commissioner*, 31 T.C. 623.

DISCUSSION

1. The sole question in this case is whether the review sought by the taxpayer in the Court of Appeals was precluded by Section 732(c) of the Code (Appendix, *infra*, pp. 15–16).

In the Tax Court, the only issue raised (R.A. 94–96) was as to the right to relief under Section 722. The sole question ultimately presented by the parties to the Tax Court for decision was, as the Court of Appeals correctly pointed out (Pet. A–3—A–5), as to the proper reconstruction of base period earnings under Section 722—*i.e.*, the determination of the appropriate "constructive average base period net income" under Section 722(a) (Appendix, *infra*, p. 13). Since the determination of that question was plainly made "necessary solely by reason of * * * section 722", the Court of Appeals was clearly correct in holding that review was prevented by Section 732(c).

2. This case involves the same general question, as to the scope and effect of the prohibition of Section 732(c) against appellate review in Section 722 cases, as was presented in four cases in which petitions for writs of certiorari were denied at the last term of this Court. *Brown Paper Mill Co.* v. *Commissioner*, 225 F. 2d 77 (C.A. 5th), certiorari denied, 358 U.S. 906; *Crowell-Collier Pub. Co.* v. *Commissioner*, 259 F. 2d 860 (C.A. 2d), certiorari denied, 358 U.S. 928; *Bradford Machine Tool Co.* v. *Commissioner*, 260 F. 2d 950 (C.A. 6th), certiorari denied, 359 U.S. 909; *Helms Bakeries* v. *Commissioner*, 263 F. 2d 642 (C.A. 9th), certiorari denied, 360 U.S. 903.

Indeed, *Brown Paper, Crowell-Collier* and *Helms Bakeries* presented a much broader and more important aspect of the scope of the prohibition of Section 732(c) than the narrow and relatively less frequent problem presented in the instant case.

3. In the early days of the litigation involving World War II relief cases, the Ninth Circuit, in *Stimson Mill Co.* v. *Commissioner*, 163 F. 2d 269, certiorari denied, 332 U.S. 824, had reviewed a question similar to the one presented in this case, and shortly thereafter the Sixth Circuit, in *Dowd-Feder, Inc.* v. *Commissioner*, 173 F. 2d 673, had followed that view as to reviewability, though somewhat reluctantly.[5]

The conflict between the decision below and *Stimson Mill* and *Dowd-Feder*[6]—which conflict, recognized by the court below (Pet. A–6), is perhaps still subsisting (compare Pet. A–6 with Pet. 10, fn. 4)—must be acknowledged. We note, however, that with the elimination of the conflict existing at the time petitions for certiorari were before the Court in *Brown Paper,*

[5] The Sixth Circuit again reviewed a similar question much more recently, in *Dayton Rubber Co.* v. *Commissioner*, 249 F. 2d 2, but without discussion of the reviewability point.

[6] There is no further conflict, as asserted (Pet. 9–10) with *Packer Pub. Co.* v. *Commissioner*, 211 F. 2d 612 (C.A. 8th). Notwithstanding certain somewhat confusing comments appearing in that opinion, by way of dictum, all that the Eighth Circuit did there was to remand the case to the Tax Court to consider the right to relief under Section 711(b)(1)(J)—which the Tax Court apparently had not passed on because not timely raised.

Crowell-Collier and *Bradford Machine*[7]—which conflict went to matters of much wider scope and effect in the application of the prohibition of Section 732(c)—there is far less compelling need now for a definitive clarification by this Court as to the reach of the prohibition of Section 732(c).

4. The number of remaining World War II relief claims is rapidly diminishing.[8] Of the 83 cases involving Sections 721 and 722 docketed in the Tax Court as of March 23, 1960, to which the taxpayer refers (Pet. 11), only approximately half that number, we are advised, involve claims for Section 722 relief.[9] Moreover, the particular controversy as to the appropriate reconstruction under Section 722, involved in this case, constitutes only a small segment of the overall problems in Section 722 cases.

---

[7] That was the conflict with the Ninth Circuit's first decision in the *Helms* case as to the reviewability of an issue under Section 722(b)(4), *Helms Bakeries* v. *Commissioner*, 236 F. 2d 3—since overruled by the Ninth Circuit itself in *Helms Bakeries* v. *Commissioner*, 283 F. 2d 642, certiorari denied, 360 U.S. 903.

[8] At the time the petition for certiorari in *Brown Paper* was before the Court at the last term, there were reported as pending between 240 and 265 cases, plus an undetermined number of cases in a certain category and of claims still at the administrative level. (See Memorandum for the Respondent in *Brown Paper Mill Co.* v. *Commissioner*, No. 351, October Term, 1958, p. 14.) As of March 23, 1960, shortly before the filing of the petition in this case, only 83 cases were reported as docketed in the Tax Court. (Pet. 11.)

[9] Controversies as to the proper method of reconstruction, such as the one submitted to the Tax Court for decision in this case, can arise only in connection with claims for relief under Section 722—not under Section 721.

CONCLUSION

Although there is a perhaps still-subsisting conflict between the decision below and decisions of the Ninth and Sixth Circuits, as indicated, the particular point involved here is quite narrow and presents a much less common and less important aspect of the scope of the prohibition of Section 732(c) against appellate review in Section 722 cases than was presented in several cases which the Court recently declined to review. Under the circumstances, and particularly in view of the rapidly diminishing number of such World War II relief cases, the need for resolution or clarification by this Court does not appear to be compelling.

Respectfully submitted.

J. LEE RANKIN,
Solicitor General.
CHARLES K. RICE,
Assistant Attorney General.
LEE A. JACKSON,
HARRY MARSELLI,
Attorneys.

JUNE 1960.

APPENDIX

Internal Revenue Code of 1939:

CHAPTER 1—INCOME TAX

* * * * *

CHAPTER 2—ADDITIONAL INCOME TAXES

* * * * *

SUBCHAPTER E—EXCESS PROFITS TAX

[As added by Sec. 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974, which provided that the new subchapter may be cited as the "Excess Profits Tax Act of 1940"]

PART I

* * * * *

SEC. 713 [as amended by Sec. 4 of the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, and Sec. 228(e)(2) of the Revenue Act of 1942, c. 619, 56 Stat. 798]. EXCESS PROFITS CREDIT—BASED ON INCOME.

(a) *Amount of Excess Profits Credit.*—The excess profits credit for any taxable year, computed under this section, shall be—

(1) *Domestic corporations.*—In the case of a domestic corporation—

(A) 95 per centum of the average base period net income,

(B) Plus 8 per centum of the net capital addition as defined in subsection (g), or

(C) Minus 6 per centum of the net capital reduction as defined in subsection (g).

* * * * *

(b) *Base Period.*—

(1) *Definition.*—As used in this section the term "base period"—

(A) If the corporation was in existence during the whole of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the period commencing with the beginning of its first taxable year beginning after December 31, 1935, and ending with the close of its last taxable year beginning before January 1, 1940; and

(B) In the case of a corporation which was in existence during only part of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the forty-eight months preceding the beginning of its first taxable year under this subchapter.

(2) *Division into halves.*—For the purposes of subsections (d) and (f), the base period of the taxpayer shall be divided into halves, the first half to be composed of one-half the entire number of months in the base period and to begin with the beginning of the base period.

* * * * *

(d) *Average Base Period Net Income—Determination.*—

(1) *Definition.*—For the purposes of this section the average base period net income of the taxpayer shall be the amount determined under subsection (e), subject to the exception that if the aggregate excess profits net income for the last half of its base period, reduced by the aggregate of the deficits in excess profits net income for such half, is greater than such aggregate so reduced for the first half, then the average base period net income shall be the amount determined under subsection (f), if greater than the amount determined under subsection (e).

* * * * *

(4) For the computation of average base period net income in the case of certain reorganizations, see section 742.

* * * * * *

(f) *Average Base Period Net Income—Increased Earnings in Last Half of Base Period.*—The average base period net income determined under this subsection shall be determined as follows:

(1) By computing, for each of the taxable years of the taxpayer in its base period, the excess profits net income for such year, or the deficit in excess profits net income for such year;

(2) By computing for each half of the base period the aggregate of the excess profits net income for each of the taxable years in such half, reduced, if for one or more of such years there was a deficit in excess profits net income, by the sum of such deficits. * * *

(3) If the amount ascertained under paragraph (2) for the second half is greater than the amount ascertained for the first half, by dividing the difference by two;

(4) By adding the amount ascertained under paragraph (3) to the amount ascertained under paragraph (2) for the second half of the base period;

(5) By dividing the amount found under paragraph (4) by the number of months in the second half of the base period and by multiplying the result by twelve;

(6) The amount ascertained under paragraph (5) shall be the average base period net income determined under this subsection, except that the average base period net income determined under this subsection shall in no case be greater than the highest excess profits net income for any taxable year in the base period. * * *

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(26 U.S.C. 1952 ed., Sec. 713.)

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SEC. 722 [as amended by Sec. 222 of the Revenue Act of 1942, *supra*, and Sec. 1 of the Act of December 17, 1943, c. 346, 57 Stat. 601]. GENERAL RELIEF—CONSTRUCTIVE AVERAGE BASE PERIOD NET INCOME.

(a) *General Rule.*—In any case in which the taxpayer establishes that the tax computed under this subchapter (without the benefit of this section) results in an excessive and discriminatory tax and establishes what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon a comparison of normal earnings and earnings during an excess profits tax period, the tax shall be determined by using such constructive average base period net income in lieu of the average base period net income otherwise determined under this subchapter. In determining such constructive average base period net income, no regard shall be had to events or conditions affecting the taxpayer, the industry of which it is a member, or taxpayers generally occurring or existing after December 31, 1939, except that, in the cases described in the last sentence of section 722(b)(4) and in section 722(c), regard shall be had to the change in the character of the business under section 722(b)(4) or the nature of the taxpayer and the character of its business under section 722(c) to the extent necessary to establish the normal earnings to be used as the constructive average base period net income.

(b) *Taxpayers Using Average Earnings Method.*—The tax computed under this subchapter (without the benefit of this section) shall be considered to be excessive and discriminatory in the case of a taxpayer entitled to use the excess profits credit based on income pursuant to section 713, if its average base period net income is an inadequate standard of normal earnings because—

* * * * *

(4) the taxpayer, either during or immediately prior to the base period, commenced business or changed the character of the business and the average base period net income does not reflect the normal operation for the entire base period of the business. If the business of the taxpayer did not reach, by the end of the base period, the earning level which it would have reached if the taxpayer had commenced business or made the change in the character of the business two years before it did so, it shall be deemed to have commenced the business or made the change at such earlier time. For the purposes of this subparagraph, the term "change in the character of the business" includes a change in the operation or management of the business, a difference in the products or services furnished, a difference in the capacity for production or operation, a difference in the ratio of nonborrowed capital to total capital, and the acquisition before January 1, 1940, of all or part of the assets of a competitor, with the result that the competition of such competitor was eliminated or diminished.

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(d) *Application for Relief Under This Section.*—The taxpayer shall compute its tax, file its return, and pay the tax shown on its return under this subchapter without the application of this section, except as provided in section 710(a)(5). The benefits of this section shall not be allowed unless the taxpayer within the period of time prescribed by section 322 and subject to the limitation as to amount of credit or refund prescribed in such section makes application therefor in accordance with regulations prescribed by the Commissioner with the approval of the Secretary. If a constructive average base period net income has been determined under the provisions of this section for any taxable year, the Commissioner may, by

regulations approved by the Secretary, prescribe the extent to which the limitations prescribed by this subsection may be waived for the purpose of determining the tax under this subchapter for a subsequent taxable year.

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(26 U.S.C. 1952 ed., Sec. 722.)

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SEC. 732 [as added by Sec. 9 of Excess Profits Tax Amendments of 1941, *supra,* and as amended by Sec. 222(c) of the Revenue Act of 1942, *supra,* by Sec. 2 of the Joint Resolution of June 30, 1945, c. 211, 59 Stat. 295, and by Sec. 203(a) of the Act of December 29, 1945, c. 652, 59 Stat. 669]. REVIEW OF ABNORMALITIES BY THE TAX COURT OF THE UNITED STATES.

(a) *Petition to Tax Court.*—If a claim for refund of tax under this subchapter for any taxable year is disallowed in whole or in part by the Commissioner, and the disallowance relates to the application of section 711(b)(1)(H), (I), (J), or (K), section 721, or section 722, relating to abnormalities, the Commissioner shall send notice of such disallowance to the taxpayer by registered mail. Within ninety days after such notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with The Tax Court for a redetermination of the tax under this subchapter. If such petition is so filed, such notice of disallowance shall be deemed to be a notice of deficiency for all purposes relating to the assessment and collection of taxes or the refund or credit of overpayments.

(b) *Deficiency Found by the Tax Court in Case of Claim.*—If the Tax Court finds that there is no overpayment of tax in respect of any taxable year in respect of which the Commissioner has disallowed, in whole or in part, a claim for refund described in subsection (a) and the Tax Court further finds that there is a deficiency for such year, the Tax Court shall

have jurisdiction to determine the amount of such deficiency and such amount shall, when the decision of the Tax Court becomes final, be assessed and shall be paid upon notice and demand from the collector.

(c) *Finality of Determination.*—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711(b)(1)(H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Tax Court.

(d) *Review by Special Division of the Tax Court.*—The determinations and redeterminations by any division of the Tax Court involving any question arising under section 721(a)(2)(C) or section 722 with respect to any taxable year shall be reviewed by a special division of the Tax Court which shall be constituted by the presiding judge and consist of not less than three judges of the Tax Court. The decisions of such special division shall not be reviewable by the Tax Court, and shall be deemed decisions of the Tax Court.

(26 U.S.C. 1952 ed., Sec. 732.)

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PART II—RULES IN CONNECTION WITH CERTAIN EXCHANGES

SUPPLEMENT A—EXCESS PROFITS CREDIT BASED ON INCOME

SEC. 740. DEFINITIONS.

For the purposes of this Supplement—

(a) *Acquiring Corporation.*—The term "acquiring corporation" means—

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(b) *Component Corporation.*—The term "component corporation" means—

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(26 U.S.C. 1952 ed., Sec. 740.)

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SEC. 742 [as amended by Sec. 228(c) of the Revenue Act of 1942, *supra*]. SUPPLEMENT A AVERAGE BASE PERIOD NET INCOME.

In the case of a taxpayer which is an acquiring corporation, its average base period net income (for the purpose of the credit computed under section 713) shall be the amount computed under section 713 or the amount of its Supplement A average base period net income, whichever is the greater. The Supplement A average base period net income shall be the amount computed without regard to subsection (h) of this section, or computed under subsection (h) of this section, whichever is the greater. The Supplement A average base period net income shall be computed as follows:

(a) By ascertaining with respect to each of its base period years—

(1) The amount of its and each of its component corporation's excess profits net income for each of its and such component corporation's taxable years beginning with or within such base period year; or, in the case of each such taxable year of the taxpayer or of such component corporation, as the case may be, in which the deductions plus the credit for dividends received and the credit provided in section 26(a) (relating to interest on certain obligations of the United States and its instrumentalities) exceeded the gross income, the amount of such excess;

(2) (A) The aggregate of the amounts of excess profits net income ascertained under paragraph (1); (B) the aggregate of the excesses ascertained under paragraph (1); and (C) the difference between the aggregates found under clause (A) and clause (B). If the aggregate ascertained under clause (A) is greater than the aggregate ascertained under clause (B), the difference shall for the purposes of

subsection (b) be designated a "plus amount", and if the aggregate ascertained under clause (B) is greater than the aggregate found under clause (A), the difference shall for the purposes of subsection (b) be designated a "minus amount".

* * * * *

(b) By adding the plus amounts ascertained under subsection (a)(2) for each year of the base period; and

(1) If the tax under this subchapter is being computed for a taxable year not beginning after December 31, 1941, by subtracting from such sum, if for two or more years of the basis period there was a minus amount, the sum of the minus amounts, excluding the greatest; or

(2) If the tax under this subchapter is being computed for a taxable year beginning after December 31, 1941, by subtracting from such sum the sum of the minus amounts. If the amount used under the preceding sentence for the lowest year is less than 75 per centum of the sum of the plus amounts reduced by the sum of the minus amounts for the other years in the base period divided by three, the amount which shall be used for such lowest year shall be 75 per centum of the amount last ascertained.

(c) By dividing the amount ascertained under subsection (b) by four.

(d) In no case shall the average base period net income be less than zero. * * *

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(h) *Increased Earnings in Last Half of Base Period.*—

(1) *General rule.*—The Supplement A average base period net income determined under this subsection shall be computed by ascertaining for each half of the base period the sum of the plus amounts determined under subsection (a) reduced if for any year in such half a

minus amount was determined by the minus amount for such year. If the amount ascertained for the second half exceeds the amount ascertained for the first half, the Supplement A average base period net income shall be the sum, divided by two, of the amount so ascertained for the second half plus one-half of such excess, except that it shall not exceed the largest plus amount determined under subsection (a) with respect to any base period year.

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(26 U.S.C. 1952 ed., Sec. 742.)

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